(3)

No. 94-1094

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In the Supreme Court of the United States

OCTOBER TERM, 1994

ROBERT B REICH, SECRETARY OF LABOR, PETITIONER

v.

CONTINENTAL CASUALTY COMPANY
AND
AMERICAN CASUALTY COMPANY OF READING,
PENNSYLVANIA, MEMBERS OF THE CNA INSURANCE
COMPANIES

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONER

1. Respondents contend (Br. in Opp. 9-10) that the Secretary's arguments for interpreting Section 502(a)(5) of ERISA, 29 U.S.C. 1132(a)(5) (1988 & Supp. V 1993), to authorize relief against nonfiduciaries were fully briefed in *Mertens* v. *Hewitt Assocs.*, 113 S. Ct. 2063 (1993), and were rejected by the Court in the course of its ruling precluding money damages under Section 502(a)(3), 29 U.S.C. 1132(a)(3). Respondents are mistaken.

a. As the Court noted in *Mertens*, the application of Section 502(a)(3) to nonfiduciaries was contested only by amici

supporting the respondent, 113 S. Ct. at 2067,[1] and for that reason the Court expressly reserved decision on the issue, *id.* at 2067-2068.

b. In *Mertens*, the Court rejected the notion that Section 502(a)(3)'s authorization of "appropriate equitable relief" includes "whatever relief a court of equity is empowered to provide"; the Court held instead that the phrase takes in only "those categories of relief that were *typically* available in equity." 113 S. Ct. at 2068-2069. Although restitution is available at law (through quasi contract), Pet. App. 3a-4a; E. Shoben & Wm. Tabb, *Cases and Problems on Remedies* 711 (1989), it is also a core concept in equity (employed principally through the remedy of constructive trust), *ibid.*; Restatement of Restitution § 160, at 640, Introductory Note 9 (1937); J. Dawson, *Unjust Enrichment* 26 (1951); *Stauffer* v. *Stauffer*, 351 A.2d 236, 241 (Pa. 1976) (constructive trust "is an equitable remedy designed to prevent unjust enrichment").

The specific remedy sought by the Secretary in this case—restitution against nonfiduciary knowing participants—is "equitable relief" under the definition adopted in *Mertens*, because it is a remedy that was typically provided at common law through the equitable doctrine of constructive trust. See Restatement of Restitution, *supra*, § 160, at 640; *id.* § 168 cmt. a, at 684; 4 A. Scott & W. Fratcher, *The Law of Trusts* § 291, at 77-78 (4th ed. 1988); G. Bogert & G. Bogert, *The Law of Trusts and Trustees* § 868, at 79, 84-85 (rev. 2d ed. 1982); 2 Restatement (Second) of Trusts §§ 288, 291 cmt. a, at 58 (1959). As the court of appeals concluded, restitution is "an equitable

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[1] The respondent in *Mertens* conceded that Sections 502(a)(3) and (a)(5) "authorize the award of equitable relief against *non-fiduciaries*, including those forms of relief, like restitution, that involve the transfer of money." Brief for Respondent at 40, *Mertens* v. *Hewitt Assocs.*, 113 S. Ct. 2063 (1993) (No. 91-1671) [hereinafter *Mertens* Resp. Br.].

remedy in a sense in which damages, though *occasionally* awarded in equity cases, are not." Pet. App. 5a.

c. *Mertens* did not address definitively the Secre-tary's argument that the text of Section 502(*l*) of ERISA, 29 U.S.C. 1132(*l*) (Supp. V 1993), presumes the avail-ability of relief against nonfiduciaries under Section 502(a)(5). The Court did reject the notion that Section 502(*l*) presumes the availability of *money damages* as an aspect of the "equitable relief" available under Section 502(a)(5). The Court reasoned that Section 502(*l*) (which bases the amount of the civil penalties it prescribes on the amount awarded against the defendant in a civil proceeding brought by the Secretary under Section 502(a)(5)) would retain meaning and scope in the absence of a cause of action for money damages so long as Section 502(a)(5) is interpreted to authorize a suit for "restitution of ill-gotten plan assets." 113 S. Ct. at 2071. The Court further observed that Section 502(*l*) would have meaning and scope "even assuming non-fiduciaries are not liable at all for knowing participation in a fiduciary's breach of duty, see *supra*, at 2067-2068, [because] cofiduciaries expressly are, see § 405(a), so there are some 'other person[s]' than fiduciaries-in-breach liable under § 502(*l*)(1)(B)." 113 S. Ct. at 2071. That interpretation was not, however, urged by the respondent.[2] Nor was it actually adopted by the Court, which made clear that it was merely "assuming" for purposes of discussion that nonfiduciaries are not liable at all under Section 502(a)(5), and referred expressly to the prior portion of the opinion (113 S. Ct. at 2067-2068) in which it had reserved judgment on that question.

[2] To the contrary, the respondent in *Mertens* affirmatively suggested that Section 502(*l*)'s reference to the "applicable recovery amount" could mean "[t]he amount of money a non-fiduciary is required to disgorge by a restitution award under § 502(a)(5)." *Mertens* Resp. Br. 40.

There are, moreover, two important factors not mentioned by the Court in *Mertens* that weigh heavily against a circumscribed reading of Section 502(*l*)'s reference to "other person." First, as we demonstrate in the certiorari petition (at 17), it is unlikely that Congress would have used the term "other person" if it had meant to restrict the scope of the civil penalty provision to cofiduciaries, since the terms "person" and "fiduciary" are separately defined in ERISA and the former is far broader than the latter. Compare 29 U.S.C. 1002(9) ("person") with 29 U.S.C. 1002(21) ("fiduciary"). Second, because Section 502(*l*)(1)(A) specifically authorizes civil penalties against fiduciaries—and because knowing participation by one fiduciary in a breach by another constitutes a breach of the former's own fiduciary duty, see 29 U.S.C. 1105(a)(1)—an interpretation of Section 502(*l*)(1)(B) that reached only fiduciaries and co-fiduciaries would render superfluous Congress's authorization of civil penalties for "knowing participation * * * by any other person."

d. The Court held in *Mertens* that Section 502(a)(3) does not authorize a suit for money damages, notwithstanding that money damages were available against nonfiduciaries at common law. In so holding, the Court did not disavow the interpretive significance of Congress's desire through ERISA to afford beneficiaries greater protection than was afforded them under the common law. See *Mertens*, 113 S. Ct. at 2071, quoting *Shaw* v. *Delta Air Lines, Inc.*, 463 U.S. 85, 90 (1983), and citing *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 114 (1989). Rather, it concluded that arguments from the "basic purpose" of ERISA could not "overcome the words of its text regarding the *specific* issue under consideration." *Mertens*, 113 S. Ct. at 2071. In this case, we are not asking the Court to elevate the Act's "basic purpose" over its text; rather, we submit, the most natural reading of the text (that "equitable relief" includes the traditional equitable remedy of restitution against a knowing participant

in a breach of trust) is promotive of Congress's intention to protect the inter-ests of plan participants and beneficiaries.

2. Respondents argue (Br. in Opp. 10) that the absence of a distinct statutory duty under ERISA to avoid knowing participation in a fiduciary breach precludes reading Section 502(a)(5) to authorize restitution against nonfiduciary knowing participants. They rely on the Court's statement in *Mertens* that trust beneficiaries had a common law remedy against nonfiduciaries "because nonfiduciaries had a *duty* to the beneficiaries not to assist in the fiduciary's breach." *Mertens*, 113 S. Ct. at 2068 n.5. The Court's apparent assumption respecting the common law, however, was incorrect. At common law, equitable restitution was not justified on the ground that the nonfiduciary had violated an independent duty. See 1 D. Dobbs, *Law of Remedies* § 4.3(2), at 597 (2d ed. 1993) (the remedy "is in no way limited to cases of wrongdoing"). Instead, the non-fiduciary's liability was a derivative of the trustee's breach of his fiduciary duties. Under the doctrine of constructive trust, "[w]here a person holding property in which another has a beneficial interest transfers title to the property in violation of his duty to the other, the transferee holds the property subject to the interest of the other, unless he is a bona fide purchaser." Restatement of Restitution, *supra*, § 168(1), at 684. In other words, a knowing transferee is treated as "[a] purchaser[] with notice, and thus as [a] mere trustee[] of the parties, who are entitled to the assets." 2 J. Story, *Commentaries on Equity Jurisprudence* § 1257, at 606 (photo. reprint 1988) (13th ed. 1886); see *id.* § 1258, at 607 ("An abuse of a trust can confer no rights on the party abusing it, or on those who claim in privity with him."). Because recovery at common law was not premised on the nonfiduciary's own breach of a legal duty, the absence of a statutory duty imposed on nonfiduciaries does not foreclose suits against nonfiduciaries to recover their unjust enrichment.

3. Respondents argue (Br. in Opp. 11) that no further review of the question presented is warranted because this Court relied on *Mertens*' discussion of that question in its subsequent decision in *Central Bank* v. *First Interstate Bank*, 114 S. Ct. 1439 (1994). In *Central Bank*, the Court adverted to the *Mertens* dictum to support the principle that the existence of a cause of action at common law provides no basis for grafting that cause of action onto an Act of Congress that does not itself provide such a cause of action. *Central Bank*, 114 S. Ct. at 1447. That principle, however, is inapposite in this case, because we do not argue that the Court should create a cause of action by implication. Instead, we argue that because the statutory phrase "appropriate equitable relief" is not self-defining, the scope of the express cause of action under Section 502(a)(5) should—consistent with standard interpretive practice—be determined with reference to the scope of "equitable relief" afforded under similar circumstances at common law. See, *e.g.*, *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. at 111-115.

4. Respondents suggest (Br. in Opp. 12) that review would be premature because there is no post-*Mertens* conflict on the question presented. As we explain in the certiorari petition (at 12), postponing review might be appropriate if the courts of appeals were analyzing the question independently, or reexamining their views on the question in light of the actual holding in *Mertens* with respect to the availability of money damages. That is not what is happening. Instead, the courts of appeals—which had previously interpreted Section 502(a)(5) as providing a cause of action against nonfiduciaries—are now barring such suits because they feel constrained to do so by *Mertens*' discussion regarding that distinct "antecedent question," even though the Court in *Mertens* expressly "reserved decision" on that question. 113 S. Ct. at 2068; see Pet. 11-13.

Because the question presented in this case was not fully briefed in *Mertens*, and was not subject to plenary review, the Court did not consider several textual and contextual factors that argue strongly in favor of interpreting Section 502(a)(5) as creating a cause of action against nonfiduciaries. Unless the Court considers the issue on its merits, the lower courts will likely continue to reject that cause of action out of hand.

5. Respondents contend (Br. in Opp. 12-14) that they did not knowingly participate in the trustees' breach of their fiduciary duties, and that they have been sued in this case merely for charging a premium that the Secretary deems to have been excessive. That is not correct. The Secretary contends that the trustees used $970,000 of plan assets to indemnify themselves against $1 million of liability, in violation of 29 U.S.C. 1110(a), 1104(a)(1)(A) and (B), and 1106(b)(1); that respondents knew that providing a $1 million policy for a $970,000 premium protected the trustees but entailed no benefit to the Plans; and that respondents agreed to provide that policy in order both to reduce their own expected losses on the Plans' prior policies and to avoid the possibility that, as a result of the trustees' lawsuit against respondents, they would be forced to reinstate the preexisting $20 million coverage. Compl. ¶¶ 11-13 (A.12); A. 57-58, 61-62; S.A. 12-24.[3] Respondents' factual culpability has yet to be tried, but the nature of the facts alleged renders this case entirely suitable as a vehicle for review of the legal question presented.

6. Contrary to respondents' contention (Br. in Opp. 14-17), there is no question that the Secretary is seeking restitution. Although he initially sought monetary damages, the

[3] There is no merit to respondents' assertion (Br. in Opp. 13-14) that the Secretary seeks to hold them liable on a theory of constructive knowledge. The Secretary contends in this case that respondents were well aware of all of the material facts respecting the trustees' wrongful actions. S.A. 15-18.

Secretary acknowledged after *Mertens* that damages were no longer available, and he made clear in his post-*Mertens* brief to the district court that the government is now seeking to recover only the amount by which respondents were unjustly enriched through their participation in the trustees' breach. See S.A. 11-12, 18-24.[4] Restitution is civil liability based on unjust enrichment. Pet. App. 6a; Shoben & Tabb, *supra*, at 711.

Respondents take pains to emphasize (Br. in Opp. 15) that they made no profit on the transaction at issue. It is irrelevant, however, whether respondents were unjustly enriched by making a profit or (as the Secretary contends) by minimizing the amount of their coverage losses. As the court of appeals recognized, there is no conceptual difference between unjust profit and unjust avoidance of loss, Pet. App. 6a, and the law has had no difficulty recognizing that the latter is equally a basis for restitution. See Restatement of Restitution, *supra*, § 1 cmt. b, at 12.[5]

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[4] In his post-*Mertens* brief to the district court, the Secretary expressed his willingness "to amend his proposed conclusions of law consistent with *Mertens*' limitations on the available remedies." S.A. 19 n.2. Although the district court did not respond to that offer—because it concluded that ERISA provides no remedies at all against nonfiduciaries—the court gave no indication that it was troubled by the absence of a formal motion to amend, cf. 6 C. Miller, *Cyclopedia of Federal Procedure* § 18.04, at 174 (3d ed. rev. 1988) ("There is recognized room for elasticity of practice in regard to amendments."), and it clearly had the authority—if the case had gone forward—to permit such amendment, see Fed. R. Civ. P. 15(a); *Foman* v. *Davis*, 371 U.S. 178, 182 (1962); see also 3 J. Wm. Moore & R. Freer, *Moore's Federal Practice* ¶ 15.08[2], at 15-53 to 15-54 (2d ed. 1994) (courts permit amendment to change a claim sounding in contract to one for reformation in equity).

[5] Contrary to respondents' assertion (Br. in Opp. 9 n.4) the court of appeals unmistakenly held that the Secretary has stated a claim for restitution (Pet. App. 5a-6a):

It is also irrelevant for present purposes whether the amount of unjust enrichment on the Secretary's underlying claim should be calculated by looking to the market value of Endorsement No. 7 at the time it was extended or, instead, to the amount of loss respondents were ultimately able to avoid. If, as respondents contend (Br. in Opp. 16-17), the Secretary should base his prayer for relief on the difference between $970,000 and the amount by which the value of Endorsement No. 7 exceeded that of the policy it replaced, the Secretary's claim can readily be adjusted on remand.[6] Regardless of how that issue is resolved, it has no bearing on the resolution of the threshold question, presented in the certiorari petition, of whether the Secretary has a cause of action against respondents at all.[7]

> But *was* the Department of Labor seeking restitution? * * * [W]hat the Department was really seeking, and what the concept of unjust enrichment and its remedial corollary restitution do encompass, was to recover a "negative unjust enrichment," consisting of the unjust avoidance of a loss.

[6] Respondents err in asserting (Br. in Opp. 15-16) that the Secretary acted inequitably by filing suit after respondents had covered the claims that arose under Endorsement No. 7. First, respondents were on notice when they paid those claims that the Secretary might bring suit against them based on the Plans' insurance policies. The agreement by which the trustees settled the suit in *Brock* v. *Hanley*, Civ. LV No. 86-421 LDG (D. Nev.), provided expressly that nothing in that settlement would preclude later claims by the Secretary based on the Plans' transactions with its insurance companies. A. 192. Second, respondents were legally obligated to cover the claims that fell within Endorsement 7. To the extent that respondents can demonstrate that the payments they made under Endorsement No. 7 exceeded those for which they would have been responsible under the Plans' prior policy, that showing will be relevant, if at all, in determining the amount by which respondents were unjustly enriched.

[7] Finally, respondents are also mistaken in their contention (Br. in Opp. 15), which is equally irrelevant for present purposes, that the Secretary's

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For the foregoing reasons and those stated in the petition, it is respectfully submitted that the petition for a writ of certiorari should be granted.

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claim cannot be one for restitution because the Secretary has not sought to have Endorsement No. 7 rescinded. "The requirement of restoration or tender is a requirement when the plaintiff's claim is the kind which, for shorthand, is said to be 'at law.' Such a requirement is not imposed when the plaintiff's suit is 'in equity.'" 1 Dobbs, *supra*, § 4.8, at 673.